

No. 11,049.

IN THE

United States Circuit Court of Appeals
FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant,

vs.

HOOPER C. DUNBAR, GORDON B. MORRIS and CRAIG C.
HORTON, Trustees of Bell View Oil Syndicate, a Trust,

Appellees.

BRIEF FOR THE APPELLEE.

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BRIEF FOR THE APPELLEE.

Opinion Below.

The District Court rendered no opinion. The findings of fact and conclusions of law are not reported. [R. 67-72.]

Jurisdiction.

This appeal involves federal unemployment taxes for the years 1936 to 1939, inclusive. Taxpayers on September 22, 1942, filed claims for refund of said taxes and interest and penalties paid thereon in the aggregate amount of \$204.41. [R. 31-35.] Said claims were rejected by the Commissioner of Internal Revenue by letter dated July 12, 1943. [R. 56-59.] On October 27, 1943, taxpayers filed a complaint in the United States District Court,

Southern District of California, Central Division, under the provisions of subsection (20) of Section 24 of the Judicial Code as amended, praying for judgment against the United States for \$204.41 plus interest. [R. 2-24.] The Government filed its answer on February 28, 1944. [R. 25-29.] The District Court on December 1, 1944, filed its findings of fact and conclusions of law and rendered judgment. [R. 67-74.] On December 18, 1944, amended judgment was entered in favor of taxpayers for \$204.41 with interest thereon according to law. [R. 75-76.] The case is brought to this Court by Notice of Appeal filed by the appellant on February 27, 1945, pursuant to the provisions of Section 128(a) of the Judicial Code, as amended. [R. 78.]

Question Presented.

The question presented is whether this Court should reverse the decision of the District Court which held that the trustees of Bell View Oil Syndicate, a trust estate, are not employees and that their remuneration is not subject to the excise tax imposed by Section 901 of the Social Security Act and Section 1600 of the Internal Revenue Code.

Statutes and Regulations Involved.

These are set forth in the appendix to the Government's brief, pages 1-3.

Statement.

This case involves only one issue:

The taxes assessed and collected by the Government under Title IX of the Social Security Act were based upon the remunerations received by appellees for their services as trustees of Bell View Oil Syndicate, a trust estate upon the ground that the trustees were employees, whereas no employer-employee relationship existed between the trust or the holders of beneficial interests and these trustees; therefore no tax should have been assessed upon the trustees' remunerations.

Statement of Facts.

The statement contained in the brief of appellant sets out the relevant facts, and they need not be repeated here.

Summary of Argument.

The tax imposed by Title IX of the Social Security Acts and Section 1600 of the Internal Revenue Code is an excise on the relation of employment. Unless the trustees here involved are employees of some employer, no tax attaches to their remuneration.

The trustees are not employees of any person. They are independent principals subject to no control except the provisions of the trust instrument and principles of equity. They are fiduciaries and not servants.

In addition, the question of the existence of an employment relation is a question of fact. That question of fact has been determined by the court below in favor of the appellees. Such determination should not be set aside here unless clearly erroneous. The facts in the record show the lower court's determination to be clearly right.

ARGUMENT.

PART I.

The Trustees of Bell View Oil Syndicate, a Trust Estate, Did Not Render Services in the Relationship of Employee to Employer Within the Meaning of the Social Security Act, and Therefore No Excise Tax Should Have Been Imposed Upon Their Remunerations.

The Social Security Act imposes an excise tax upon employers. For the years from 1936 to 1939 this provision is contained in the Act itself, at 42 U. S. C. A., Sec. 1004, and for subsequent years it is incorporated into the Internal Revenue Code at Section 1600. The excise is placed upon an employer "with respect to having individuals in his employ." The Act (42 U. S. C. A., Section 1011(b)) defines "employment" to mean "any service, of whatever nature, performed within the United States by an employee for his employer, * * *." The Act attempts no definition of either "employer" or "employee" as those words are used in the Act. Nowhere in the Act is there any indication that the terms "employer," "employee" or "employment" are used in other than their natural and normal signification.

It is well settled that the natural and usual meaning of plain terms is to be adopted as the legislative intent in a statute in the absence of a clear showing that something else was intended. *United States v. First National Bank*, 234 U. S. 245, 34 S. Ct. 846, 58 L. Ed. 1298; *Avery v. Commissioner of Internal Revenue*, 292 U. S. 210, 54 S. Ct. 674, 78 L. Ed. 1216. Congress is presumed to have used a word in a statute in its usual and well settled sense. *United States v. Stewart*, 311 U. S. 60, 61 S. Ct. 102, 85

L. Ed. 40. Consequently when Congress used the term "employee" in the Social Security Act, without more, it must have intended that the term be understood according to its common acceptation, and with reference to the common law wherein the term "employee" has acquired a definite and well established meaning. Indeed, where the question has arisen in regard to the Social Security Act, the courts have defined the term "employee" in accordance with the common law concept. In *Texas Co. v. Higgins* (C. C. A. 2, 1941, 118 F. (2d) 636, at page 638, Judge Learned Hand said:

"Were the question presented to us for the first time, we should have no doubt that Thomas and his assistants were not 'employees' of the plaintiff; the act appears to take over the term as the common law knew it, and at common law they would not be employees. The regulation is in harmony with this assumption, for it enumerates the generally accredited determinants in such cases, of which the most important is the putative employer's control over the employee's business. * * *

It was there held that the individual rendering services was not an employee under the Social Security Act because the element of control by his alleged employer was lacking.

Persuasive evidence as to the meaning of "employee" as that term was used by Congress in Title IX of the Social Security Act is the interpretation placed upon the word by the regulations promulgated thereunder by the Treasury Department. (Regulations 107, Section

403.204.) This is the definition contained in the Commissioner's regulations:

"Every individual is an employee if the relationship between him and the person for whom he performs services is the legal relationship of employer and employee. * * *

"Generally such relationship exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. That is, an employee is subject to the will and control of the employer not only as to *what* shall be done but *how* it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if he has the right to do so. The right to discharge is also an important factor indicating that the person possessing that right is an employer. * * *" (Italics in original.)

Thus the regulations do no more than reiterate the familiar common law principles, and they place particular emphasis upon control or the right to control as the test which evidences the relationship.

The Government here, however, is contending for a different definition. On page 10 of its brief it is stated:

"It is the position of the Government, however, that the proper meaning of the term is not to be determined solely by reference to common law standards, but rather must be found by considering the purposes of the Act and the circumstances in which it is sought to be applied."

Since the purpose of the Act is to alleviate unemployment as much as possible, the Government argues that if the person rendering services is subject to the vicissitudes of idleness or lack of occupation, even in a purely hypothetical sense, as in the case of these trustees, he is an employee within the meaning of the Act, although as to him the incidents of the employment relation in the usual and ordinary sense do not exist. This definition of the term "employee" is not supported by the Act itself, by the regulations of the Treasury Department, or by the decided cases.

It has been uniformly held by the courts in construing the Social Security Act that the words "employer," "employee," and "employ," used in the statute, are intended to describe the conventional relation of employer and employee. *Texas Co. v. Higgins*, *supra*; *Indian Refining Co. v. Dallman*, 119 F. (2d) 417, (C. C. A. 7, 1941), affirming D. C. 31 F. Supp. 455; *United States v. Griswold, et al.* (C. C. A. 1, 1941), 124 F. (2d) 599; *Anglim v. Empire Star Mines Co.* (C. C. A. 9, 1942), 129 F. (2d) 914; *Magruder, Collector, v. Yellow Cab Co. of D. C., Inc.* (C. C. A. 4, 1944), 141 F. (2d) 324; *United States v. Aberdeen Aerie No. 24 of Fraternal Order of Eagles* (C. C. A. 9, 1945), 148 F. (2d) 655; *Burruss, et al. v. Early*, 44 Fed. Supp. 21. Whenever the test has not been met it has been held that the individual was not an employee. And as we have pointed out above, the most important determinant is the existence of the right to control the putative employee. If there is no right to control an individual by the person who is alleged to be his employer, he is not an employee, and this is so whether the alleged employer be an individual, a corporation, or an association taxable as a corporation for Federal Income Tax

purposes. Appellant falls far short of making its case by asserting that this trust is an association within the meaning of Section 1101(a) of the Internal Revenue Code.

The facts here are clear and undisputed. These trustees acquired legal title to the trust estate under a written declaration of trust dated January 20, 1922. [R. 30, 35.] The important terms of the trust declaration are as follows: The instrument gives the trustees exclusive management and control of the trust estate with power to make contracts and conveyances relating to the trust estate, to compromise claims, to hold legal title to the trust estate, to employ counsel, to develop and operate oil properties and to act by majority vote of the trustees. [R. 37, 39.] The remaining trustees are given power to fill any vacancies occasioned by the death or resignation or refusal to act of any trustee. [R. 41.] The trustees are given power to fix their own remunerations, provided that their fees and other office and overhead expenses are not to exceed ten per cent of the gross income of the trust. [R. 40.] The trustees are not to be liable for any mistake in judgment and their liability is confined to willful breach of the trust imposed upon them under state law. [R. 41.] They have no power to bind unit holders. [R. 40.] They are appointed for life or the duration of the trust. [R. 37.] They may employ and remove such officers, agents and employees as they deem necessary. [R. 46.] The only voting right held by the holders of the beneficial interests is in respect to consenting to the alteration or amendment of the trust agreement or the termination thereof. [R. 48.] The trustees in the management of the trust are not subject to direction or control by the unit holders, by the trust estate, or by any other

person. The District Court so found in its Findings of Fact. [R. 70.] In all ways they conduct themselves as principals and legal owners of the trust estate, and this also was found by the court below. [R. 70.] Such finding accords with both the evidence and the law, and should therefore be taken as conclusive in this case.

Appellant cites *Morrissey v. Commissioner*, 296 U. S. 344, 56 S. Ct. 289, 80 L. ed. 263. The Supreme Court there, in dealing with a business trust, at page 359 said that the trustees thereof act "in much the same manner as directors." See also *Hecht v. Malley*, 265 U. S. 144, 161, 44 S. Ct. 462, 68 L. ed. 949.

The Commissioner of Internal Revenue has consistently adhered to the view that directors of corporations are not employees. Reg. 107, Sec. 403.204. Thus the fact that these trustees constitute an association for certain federal tax purposes is immaterial.

The trust here is simply the collective designation of the trustees. It is not a separate legal entity. *Hecht v. Malley, supra*. In making contracts for the trust and in all their other actions, these trustees do not act as agents. They are principals and are personally liable upon their contracts, except so far as they protect themselves by contract against individual liability. As a matter of fact, they are the trust.

The trial judge in this case made the following finding of fact, which apparently is not objected to or questioned by the Government. [R. 70.] "They [the trustees] acted at all times as principals and as owners of the trust estate. They were not subject to direction or control by any other person or persons and in performing their duties under the trust instrument they did not act as the agents or

employees for any person or persons." It has been held by this Court that the existence of an employment relation is a question of fact. *Swayne & Hoyt, Inc. v. Barsch* (C. C. A. 9), 226 Fed. 581. Consequently, the finding of the Court below was a finding of fact which should not be set aside. A finding of fact is not to be set aside "unless clearly erroneous." (Rule 52, Rules of Civil Procedure for the District Courts of the United States.)

The Restatement of the Law of Agency, Section 14(c) states:

"There are many relationships in which one acts for the benefit of another which are to be distinguished from agency by the fact that there is no control by the beneficiary. * * * A trustee, that is, one holding property in trust for another and subject to equitable duties to deal with the property for the other's benefit, may or may not be subject to control in the management of the property by the one for whose benefit he is required to act. If he is so subject, he is also an agent, and the Rules stated in the Restatement of this subject apply to him."

Under the foregoing rule these trustees are neither agents nor employees of the trust. When the precise question here involved was presented to the Court, it was held that the trustees were not employees within the purview of the Social Security Act. *United States v. Griswold, supra.* Appellant apparently concedes that the facts in that case are not distinguishable from the facts here. The trust there was a Massachusetts business trust, and was treated as a corporation for taxing purposes under the Internal Revenue Code. The Circuit Court held an employee to be one who meets the established concept of

the legal relationship of employer and employee. At page 601, the Court said:

“The relationship of employer and employee in the ordinary sense does not exist here. These trustees render services and receive compensation, but we do not feel that they are subject to such supervision and control as to make them employees within the scope of the Congressional intent.”

The Supreme Judicial Court of Massachusetts has reached the same conclusion under the Massachusetts Unemployment Compensation law. *Griswold, et al. v. Director of Division of Unemployment Compensation and Division of Employment Security*, 315 Mass. 371, 53 N. E. (2d) 108. The Court said in part:

“The obligation of an employer to the unemployment fund is based upon the relation of employer and employee; and where, as here, there is nothing in our law indicating anything to the contrary, the existence of such a relationship must be determined by the principles of the common law.” (p. 109.)

“* * * The trustees are not subject to any control of the shareholders. They have no superiors in the conduct of the business of the trust. They manage the affairs of the trust in accordance with the agreement and declaration of trust as they in their discretion and judgment deem appropriate. They are the masters and principals in the business of the trust. They have the legal title to the trust property and none other than the trustees can do any act that affects the rights or property of the trust. * * *”

The Court concluded:

“The trustees [of a business trust] are not employees of such a trust.” (p. 109.)

Appellant cites *Carroll v. Social Security Board*, 128 F. (2d) 876, as being in opposition to the views which have been held by the cases above cited. A reading of the case, however, shows that the court was not departing from the principles which have generally been held. There was no serious contention in that case that the individual in question was not an employee. The defense rather was that he was an employee of the State of Illinois, and as such, exempt from the Act under 42 U. S. C. A., Sec. 1107(c)(6). It was held that the bank and not the State was the employer of this admitted employee. The Court distinguishes the case of *United States v. Griswold, supra*, upon the ground that the right to control by the putative employer which was lacking there, was present, pointing out that the individual in question was subject to removal at the pleasure of the bank's creditors. The cases of *Lehigh Valley Coal Co. v. Yensavage*, 218 Fed. 547, and *National Labor Relations Board v. Hearst Publications, Inc.*, 322 U. S. 111, 64 S. Ct. 851, 88 L. Ed. 1170, cited by appellant, were decided with reference to entirely different statutes enacted under different conditions and for different purposes. In view of the well-settled construction by the courts of the Social Security Act, these cases cannot add or detract from the definition of "employee" as established by the decisions under this Act.

Appellant also cites *Grace v. Magruder*, 148 F. (2d) 679 (App. D. C.), and *United States v. Vogue, Inc.*, 145 F. (2d) 609 (C. C. A. 4). The first case involved coal hustlers and the second seamstresses. In both cases, the individuals worked under conditions of employment, whereby their respective employers, had they so desired, would have been able to have exerted substantial control over them. In addition, in the *Vogue* Case the

employer furnished the working quarters and even a sewing machine to one of the women. They observed the same working hours as the regular employees and had no key to the establishment. The work was furnished by the employer, who collected from the customer and paid the seamstresses a percentage of collections. This Court distinguished the *Vogue* Case in *United States v. Aberdeen Aerie No. 24 of Fraternal Order of Eagles, supra.* In the *Grace* case, although no express contract of employment existed, the court found the hustlers worked under "compelling supervision" as a result of the practice of the employer in paying them. These cases, it is submitted are distinguishable upon the facts and offer no guide to the nature of the relationship occupied by these trustees, in respect to whom entirely different circumstances exist.

It is also contended by the appellant that the Senate Finance Committee having twice failed to take favorable action on a bill which would have clarified the status of trustees of Massachusetts business trusts, Congress is thereby presumed to have approved S. S. T. 136, 1937-1 Cum. Bull. 377, wherein it is contended by the Commissioner that such trustees are employees. There is no indication that the lower house of Congress was ever made aware of the existence of this bill. In the Senate Hearings before the Committee on Finance on H. R. 6635, Social Security Act Amendments, 76th Cong. 1st Sess., pp. 105-114, it affirmatively appears that the sponsor of the bill had not presented it to the House Ways and Means Committee because there was not time enough. No bill was introduced on the floor of the lower house. Thus, from the non-action of a committee of one of the houses of Congress, the appellant presumes the intent of Congress is evidenced.

The additional fact appears that the bill as presented to the Committee was defective. In the letter of the Treasury Department upon the bill (84 Cong. Record, Part 8, pp. 9030, 9031) it is pointed out to the Committee that the remuneration of trustees would be included for purposes of the benefits provided by Title II of the Act, but would not be subject to the taxes imposed by Title VIII of the Act (subsequently incorporated into the Internal Revenue Code). Thus, such trustees, the Treasury contended, would be eligible for benefits under the Act, without being subject to the tax which is imposed. It may well be that the only intent of the Committee was to avoid such an incongruous result.

However, if presumptions are to be indulged in, it would seem that the construction placed upon the Act by the taxpayers is the one of which Congress has indicated approval. The published regulations reiterate the common law definition of the term "employee." (Reg. 107, Sec. 403.204.) It is much more likely that Congress would be acquainted with them rather than with an obscure and inconsistent ruling. By failing to amend the Act, Congress has indicated its approval of the interpretation of the term "employee" contained in the regulations and the decided cases. It has been stated as a rule of construction that where Congress has not amended a law, it must be taken that the construction placed upon it by the courts is the true construction, acceptable to the legislative as well as the judicial branch of the Government. *Baltimore & Ohio Railroad Company v. John Baugh*, 149 U. S. 368, 13 S. Ct. 914, 37 L. Ed. 772. As we have shown the courts have followed the usual common law definition of the term "employee." In the *Griswold Case*, at page 601, the Court expressly declared S. S. T. 136, 1937-1 C. B. 377 to be an erroneous interpretation of the statute.

Finally, it appears that the contention of the Government that a new definition of the term "employee" should be adopted, because of the remedial purposes of the Social Security Act, has already been answered by this Court in the case of *Anglim v. Empire Star Mines Co., Ltd.*, *supra*. In that case the individuals involved were miners and might with much more reason be thought to be employees than these trustees who are more nearly in the nature of partners or independent business enterprisers. However, this Court applied the established common law test and held the individuals not to be employees because the alleged employer had no right to control their acts.

Speaking through Judge Healy, the Court states:

"* * * It [the Government] argues further that since the tax provisions are integral parts of the remedial system of old age and survivors insurance enacted to promote the general welfare, the term 'employee' should have a liberal interpretation to effect the legislative purpose.

"However, in defining the required relationship, and in drawing the distinction between an employee and an independent contractor, the regulations do no more than reiterate the familiar principles of the common law. Cf. Restatement, Agency, Secs. 2, 220. Such has been the view uniformly taken of them by the courts in cases arising under the statute. *Texas Co. v. Higgins*, 2 Cir., 118 F. (2d) 636; *Indian Refining Co. v. Dallman*, 7 Cir., 119 F. (2d) 417, affirming D. C., 31 F. Supp. 455; *Williams v. United States*, 7 Cir., 126 F. (2d) 129; *Jones v. Goodson*, 10 Cir., 121 F. (2d) 176.

"* * * We are not unmindful of the beneficent purposes of the Act, but the extension of its benefits to wider fields is not the business of the courts."

It is to be noted that the cases which speak of the Congressional intent in the light of the remedial and beneficial purpose of the Act have nevertheless found as a matter of fact that the right to control did exist, and have done no more than apply the usual common law test. Regarding intent, however, it is unrealistic, to say the least, to assume that the framers of the Act had in mind independent business enterprisers such as these trustees.

Conclusion.

The decision of the Court below is right and should be affirmed.

Respectfully submitted,

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